Supreme Court of the United States

OCTOBER TERM, 1941.

No.

In the Matter
of
GEORGE A. CARDEN,
Bankrupt.

McCLAVE & COMPANY,
Petitioners,
GEORGE A. CARDEN, DANIEL LOEB and
Petitioning Creditors,
Appellees.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

I.

Statement of the Case.

The essential facts have been set forth in the foregoing petition. They may briefly be epitomized.

The bankrupt has joined together with a number of creditors to effectuate a plan which, if successful, will deprive the $660,000 judgment owned by petitioners of its seniority under the state court receivership. Their *modus operandi* was to employ a patently invalid and abandoned petition, filed six years before, as the springboard of an adjudication in bankruptcy. If sustained, the adjudication will then have been made upon an alleged petition which antedated the state court receivership.

Petitioners have moved to preserve the lien of their judgment by attacking the validity of the ancient alleged petition and, derivatively, the proceedings thereunder. The lower courts have held that petitioners are not the proper parties on whose behalf such a motion can be made; that, although the sole purpose of this entire bankruptcy proceeding is, concededly, that of destroying the priority of their lien, they are to be excluded from participation and forced to remain passive observers of the destruction of their rights.

II.

Specification of Errors.

The Circuit Court of Appeals affirmed the denial of petitioners' motion to vacate the bankruptcy proceedings upon the ground that the Chandler Act precluded such a motion if made by a creditor. That decision was erroneous for three reasons:

1. It ignored the fact, and the legal implication from the fact, that the alleged bankruptcy petition was jurisdictionally defective on its face.
2. It ignored the practice of bankruptcy courts to permit motions to vacate proceedings to be made by those not expressly authorized by the statute in any situation in which it would appear that the proceeding ought not to be allowed to proceed.
3. It ignored the manifest injustice of construing the Chandler Act in such a way as to deprive petitioners of a valuable right which had vested under the old Bankruptcy Act effective on the date of the filing of the alleged petition.

Petitioners urged each of these three contentions in both of the lower courts.

POINT I.

Petitioners' motion to dismiss should have been granted by reason of the fact that the alleged petition in bankruptcy was jurisdictionally defective on its face.

The alleged petition in involuntary bankruptcy was not filed until approximately one year after the dates upon which it had been signed by the several petitioning creditors. Accordingly, it was jurisdictionally defective for failure to allege the occurrence of an act of bankruptcy within four months next preceding the date of filing. Bankruptcy Act, Section 3 (b); *In re D. F. Herlehy Co.* (D. C., N. D. New York), 247 Fed. 369; *In re McGraw* (D. C., N. D. West Virginia), 254 Fed. 442, *In re Day* (D. C., D. Maryland), 22 Fed. Supp. 946.

A bankruptcy petition which is jurisdictionally defective on its face can be attacked by anyone. It should be vacated by the court *sua sponte*. *In re Ettinger* (C. C. A., 2nd Cir.), 76 Fed. (2nd) 741; *Chicago Bank of Commerce* v. *Carter* (C. C. A., 8th Cir.), 61 Fed. (2nd) 986; *In re American Bond & Mortgage Co.* (C. C. A., 7th Cir.), 61 Fed. (2nd) 875, aff'd 289 U. S. 165; *In re Vassar Foundry Co.* (D. C., E. D. Michigan), 293 Fed. 248, aff'd (C. C. A., 6th Cir.) 2 Fed. (2nd) 240; *In re Day* (D. C., D. Maryland), 22 Fed. Supp. 946; *In re New York Tunnel Co.* (C. C. A., 2nd Cir.) 166 Fed. 284.

A single illustration of the application of this rule under the old Bankruptcy Act forms a perfect parallel to the instant situation. Thus, it had always been the rule under the old Act that a creditor would not be permitted to attack a voluntary, as distinct from an involuntary petition. Yet the creditor was permitted to attack a voluntary petition which was jurisdictionally defective on its face in situations wherein, if the defect had been less than

jurisdictional, he would have been barred. *In re Ettinger* (C. C. A., 2nd Cir.), 76 Fed. (2nd) 741; *Chicago Bank of Commerce* v. *Carter* (C. C. A., 8th Cir.), 61 Fed. (2nd) 986; *In re American Bond & Mortgage Co.*, (C. C. A., 7th Cir.), 61 Fed. (2nd) 875, aff'd 289 U. S. 165; *In re Vassar Foundry Co.* (D. C., E. D. Michigan), 293 Fed. 248, aff'd (C. C. A., 6th Cir.), 2 Fed. (2nd) 240.

Finally, a bankruptcy petition which is jurisdictionally defective on its face cannot be redeemed by subsequent amendment or converted into a voluntary petition *nunc pro tunc*. If its defect be of a jurisdictional order, an amendment could render it valid only as of the date of the amendment itself, leaving unaffected whatever liens or other rights may have vested in the interim. *In re Condon* (C. C. A., 2nd Cir.), 209 Fed. 800; *In re Louisell Lumber Co.* (C. C. A., 5th Cir.), 209 Fed. 784; *Hovland* v. *Farmers' State Bank* (C. C. A., 8th Cir.), 10 Fed. (2nd) 478; *In re Hollywood Land & Water* Co. (D. C., S. D. Florida), 41 Fed. (2nd) 778; *In re Triangle S. S. Co., Inc.* (D. C., S. D. New York, per Mayer, D. J.), 267 Fed. 303.

The Circuit Court treated this situation cavalierly. It stated, simply, "that it is, of course, undoubted that the court had jurisdiction of the petition when filed" (page 48). The decisions above cited are to the contrary. If it were the law that the jurisdictional requirements of the Bankruptcy Act could be met, *ipso facto*, through the device of a paper's simply denominating itself a petition in bankruptcy (despite its failure to allege the facts required by the Bankruptcy Act), then the piece of paper in this case (which did not allege the commission of an act of bankruptcy within four months next preceding the date of filing) satisfied the jurisdictional requirement. But otherwise it did not.

POINT II.

Petitioners' motion to dismiss the bankruptcy proceedings should have been granted upon the ground that the bankruptcy proceedings ought not to be allowed to proceed.

There are two questions to be considered: one of power and one of the propriety of its exercise.

In *Securities & Exch. Com'n.* v. *U. S. R. & Imp. Co.*, 310 U. S. 434 (decided under the Chandler Act), this Court announced the rule in the following language (pages 457-8):

> "And it has long been the practice of bankruptcy courts to permit creditors or others not entitled to file pleadings or otherwise contest the allegations of a petition to move for the vacation of an adjudication or the dismissal of a petition, on grounds, whether jurisdictional or not, that the proceeding ought not to be allowed to proceed."

Since the Congress which enacted the Chandler Act was presumably aware of the existence of the rule referred to by this Court, it is reasonable to assume that its failure to specifically confer such rights upon creditors was due to its reliance upon the reserve power of the bankruptcy court to accord such a status to them whenever the situation required it.

We can conceive of no situation more clearly requiring the exercise of that power than the one here presented. Creditors, who had attested their own recognition of the insufficient character of the pretended 1933 petition by causing a state receivership to be extended to their own judgments, have sought to "revive" the pretended petition some six years later for the concededly sole purpose of destroying the lien of petitioners' judgment. The circumstance that the alleged bankrupt was a party to that

plan sufficiently accounts for his own failure to challenge the validity of the proceedings. In this situation, a rule which would limit the right of challenge to the bankrupt, while withholding it from these lien creditors, would have this anomolous character: that it would endorse a collusive proceeding by confining the participants to those interested in obtaining the same result, while excluding the only ones having a contrary stake! By such exclusion (as the opinion of the Circuit Court itself avows) petitioners' judgment lien may be destroyed in consequence of proceedings in which they were not even permitted to participate (page 48).

Accordingly, the exclusion of petitioners from the bankruptcy proceedings in which the fate of their judgment lien is to be determined must be the full equivalent of the production of the famous Shakespearean tragedy without Hamlet.

POINT III.

If petitioners' motion to dismiss the bankruptcy proceedings were precluded by the Chandler Act, then it should have been determined and granted under the old Bankruptcy Act.

This alleged petition in bankruptcy was filed in 1933 under the Old Bankruptcy Act. This Court has held that the rights of creditors, both as against the estate and as among themselves, are fixed as of the date of the filing of the petition. *U. S.* v. *Marxen*, 307 U. S. 200, 207. Since it is conceded that petitioners' motion to vacate these bankruptcy proceedings would have been granted under the old Bankruptcy Act, the question now arises whether that right is destructible by reason of a statute which only became effective some five years after the alleged petition had been filed, and approximately a year after the lien under the petitioners' judgment had vested.

The situation cannot be disposed of via the simple device of characterizing petitioners' rights under the old Act as procedural and then asserting that matters of remedy do not partake of the immunity of a vested right. As we have seen, the Circuit Court itself expressed its recognition of the importance of petitioners' right to challenge the validity of the bankruptcy proceedings (page 46). Upon that right the validity of their judgment lein in excess of $660,000 directly depends. In such a situation, the withdrawal of the essential remedy must necessarily work a retroactive destruction of the substantive right which is dependant thereon.

This doctrine was expressed by Judge Cardozo in *Jacobus* v. *Colgate*, 217 N. Y. 235, as follows (p. 241): "that statutes which take away every remedy for past wrongs as distinguished from statutes which merely change the remedy are condemned as unconstitutional."

The impropriety of permitting this later statute to deprive petitioners of the important remedy (and derivative substantive right) which they had enjoyed under the old Act may be expressed in either of two ways. It might be said, in the language of this same Circuit Court in another case, that retroactive application of a statute will be denied whenever such application would "disturb vested rights". *In re John G. Gasteiger & Co. Inc.*, (C. C. A., 2nd Cir.), 25 Fed. (2nd) 642, 643. Or it might alternatively be said that a retroactive application of the statute would be unconstitutional pursuant to the reasoning of Cardozo, J.

Whichever rubric be employed, the conclusion must be the same. "No writ, no right". A remedy so indispensable to the preservation and defense of a vested right must be immune to destruction by a statute becoming effective more than five years after the date of the filing of the alleged petition.

Conclusion.

As we have seen, the situation presents important questions with respect to the interpretation of a federal statute. Neither of these questions has been passed upon by this Court directly. Analogical decisions handed down before the enactment of the Chandler Act indicate the decision of the Circuit Court to have been erroneous.

These questions must inevitably be passed upon and determined by this Court at some time. The substantial character of petitioners' interest as the owner of a judgment in excess of $660,000 makes it seem desirable that the matters be determined now since they are directly raised on this record.

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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Attorney for Petitioners.